Bloomberg

Yahoo, Dell Swell Netherlands' $13 Trillion Tax Haven

By Jesse Drucker - Jan 23, 2013

Inside Reindert Dooves's home, a 17th- century, three-story converted warehouse along the Zaan canal in suburban Amsterdam, a 21st-century Internet giant is avoiding taxes.

The bookkeeper's home office doubles as the headquarters for a Yahoo! Inc. (YHOO) offshore unit. Through this sun-filled, white- walled room, Yahoo has taken advantage of the law to quietly funnel hundreds of millions of dollars in global profits to island subsidiaries, cutting its worldwide tax bill.

The Yahoo arrangement illustrates that the Netherlands, in the heart of a continent better known for social welfare than corporate welfare, has emerged as one of the most important tax havens for multinational companies. Now, as a deficit-strapped Europe raises retirement ages and taxes on the working class, the Netherlands' role as a $13 trillion relay station on the global tax-avoiding network is prompting a backlash.

The Dutch Parliament is scheduled to debate the fairness of its tax system today. Lawmakers from several parties, including members of the country's governing coalition, say they want to remove a stain on the nation's reputation.

"We should not be a tax haven," said Ed Groot, a parliament member from the Labour Party, which along with the People's Party for Freedom and Democracy took power in November. Both ruling parties are "fed up with these so called PO Box companies," he said. "If they go somewhere else we are not sorry at all because they spoil the name of Holland. Otherwise you can wait for retaliation measures and this we don't want."

War Declaration

Last month, the European Commission, the European Union's executive body, declared a war on tax avoidance and evasion, which it said costs the EU 1 trillion euros a year. The commission advised member states -- including the Netherlands -- to create tax-haven blacklists and adopt anti-abuse rules. It also recommended reforms that could undermine the lure of the Netherlands, and hurt a spinoff industry that has mushroomed in and around Amsterdam to abet tax avoidance.

Attracted by the Netherlands' lenient policies and extensive network of tax treaties, companies such as

Yahoo, Google Inc. (GOOG), Merck & Co. and Dell Inc. have moved profits through the country. Using techniques with nicknames such as the "Dutch Sandwich," multinational companies routed 10.2 trillion euros in 2010 through 14,300 Dutch "special financial units," according to the Dutch Central Bank. Such units often only exist on paper, as is allowed by law.

'Harmful Role'

The EU's 27 member states had accumulated an annual 519.5 billion euro budget deficit as of the second quarter of 2012, according to Eurostat. In response, Spain is slashing teacher salaries and Greece is cutting funding for public hospitals and prescription drugs. The Netherlands had a deficit of 24.9 billion euros.

"Governments around the world have to cut budgets and at the same time multinational companies are avoiding taxes," said Arnold Merkies, a Dutch parliament member from the Socialist Party.

Merkies recently sent questions to the state secretary for finance about the Netherlands' role in enabling a tax-avoidance strategy used by Google, after Bloomberg News reported in December that the company had funneled almost $10 billion through a Dutch shell company en route to Bermuda in 2011. The move cut the company's worldwide tax bill by $2 billion that year.

"We connect the tax havens here," Merkies said. "We have a harmful role in the world and have a responsibility toward the rest of the world."

OECD Proposal

Profit shifting into tax havens by corporations costs the U.S. $90 billion a year, according to Kimberly Clausing, an economics professor at Reed College in Portland, Oregon. The U.S. faces a projected budget deficit of almost $1 trillion in fiscal 2013.

The Paris-based Organization for Economic Cooperation and Development -- which sets standards for how multinational companies allocate taxable income around the world -- is also tackling the issue. It's discussing a proposal that could make it harder for companies to move profits through the Netherlands into island tax havens.

Anger over corporate tax avoidance is spreading throughout Europe. On Jan. 31, the U.K. Parliament is scheduled to hold its second hearing on the issue. At a November hearing, members of Parliament quizzed executives from Google and Starbucks Corp. about their use of Netherlands subsidiaries to cut taxes.

'Applicable Taxes'

Yahoo's offshore operations cut its taxes by $42.8 million in 2011, U.S. securities filings show. Last February, the company reported a dispute with the U.S. Internal Revenue Service regarding its overseas arrangements. It didn't disclose the amount at stake.

"Yahoo! pays all applicable taxes in every jurisdiction where we operate," said Sara Gorman, a spokeswoman for the company, based in Sunnyvale, California. She didn't respond to a detailed list of questions about Yahoo's Dutch tax-cutting arrangements.

By routing profits through the Netherlands en route to island havens, companies receive an important benefit: They generally don't have to pay taxes on payments leaving or entering the country.

Technology and pharmaceutical companies often seek to reduce their tax bills by paying royalties to license patent rights from offshore subsidiaries.

Withholding Tax

Such transactions could incur a cost: many developed nations impose a withholding tax -- sometimes as high as 33 percent -- on royalties leaving for zero-tax locales with which they don't have tax treaties, such as Bermuda and the Cayman Islands. By contrast, the Netherlands doesn't impose withholding taxes on royalties leaving the country, regardless of their destination.

Countries often either eliminate or reduce those taxes when such payments head to a treaty partner. The extensive Dutch treaty network thus protects payments on the way into the country as well.

The Netherlands' role in facilitating tax avoidance began in force in the late 1970s, when it started so-called advance- pricing agreements to attract multinational companies, said Francis Weyzig, chair of Tax Justice Network Europe, who is finishing a Ph.D. thesis at Radboud University on Dutch tax policy.

Under such agreements, multinational companies agree to leave a tiny amount of income in the Netherlands to be taxed in exchange for being permitted to route profits through the country. This remainder left for the revenue authorities in the Netherlands is known to tax planners as "the Dutch Turn."

'All Upfront'

Yahoo, for instance, has an agreement to pay taxes equal to about 1.35 percent of the unit's total revenue, said the soft- spoken Dooves, who has run the Yahoo unit since 2007. He previously worked as treasurer for a Dutch packaging company for almost 15 years.

"The benefit of the Netherlands is that you know all upfront," Dooves said in his high-ceilinged home office in the town of Koog aan de Zaan, overlooking a placid commercial street with a scooter store, bakery and Thai restaurant.

Records show that the Yahoo unit reported Dutch income taxes in 2009 of 1.28 million euros -- out of the 101.5 million euros in royalties it funneled through the subsidiary that year.

That's a small price to pay. In return, Yahoo can move profits to virtually any destination without paying a withholding tax.

Nothing Illegal

Tax avoidance has fostered a sizable industry in the Netherlands of so-called trust firms, generating about 1 billion euros in annual tax revenues and about 3,500 jobs, according to a 2009 study by SEO Economic Research. Local companies such as Intertrust Group Holding SA and TMF Group set up high-priced mailboxes for multinational companies, often by providing them with an address at their gleaming, high-rise office buildings near the Amstel River and Amsterdam's massive soccer arena. Trust firms also provide non tax-related services, such as bookkeeping and payroll administration.

Jan Reint de Vos van Steenwijk, managing director of TMF Holding BV, said he expects the Dutch government to wait until the release this spring of a research report on the economic impact of the corporate services industry before taking any action.

"The benefits to Holland are employment, high-level tax advisers," said Jos Peters, tax director for Merlyn Tax Solutions & Royalty Conduit Services in Rotterdam. "They come to us and why should we refuse this? We are not doing anything illegal or immoral."

Blackstone Purchase

In December, Blackstone Group LP (BX), the New York-based private equity giant, announced it would buy one of the biggest such firms, Intertrust, for $833 million, according to a person with knowledge of the deal.

Merck, the maker of diabetes drug Januvia and asthma treatment Singulair, lists 54 subsidiaries in the Netherlands. From 2002 to 2010 the company routed more than 7 billion euros in royalties, mostly from European sales, to Bermuda via an Amsterdam subsidiary called Crosswinds BV.

The unit -- which had no employees -- was named Crosswinds to conjure the image of royalties crossing in and out "like wind blowing," said a person familiar with the matter.

In late 2010, after Merck acquired Schering Plough Corp., it stopped using Crosswinds to route royalties. Merck cut $1.9 billion off its tax bill that year because of its offshore arrangements, securities filings show.

Ronald Rogers, a spokesman for Merck, based in Whitehouse Station, New Jersey, declined to discuss its tax strategies.

"Merck files its income tax returns in accordance with all applicable laws and regulations," Rogers said.

Double Non-Taxation

One purpose of tax treaties is to prevent companies from paying tax twice in two different countries on the same profit.

Dell, however, uses the Netherlands to avoid paying income taxes in either place. The world's third-largest personal- computer maker has avoided about $4 billion in income taxes since 2004, thanks partly to its use of a Dutch unit.

The subsidiary, called Dell Global BV, paid income taxes at a rate of 1/10 of 1 percent on profits of about $2 billion in 2011, the most recent year for which records are available. That means the unit took credit for almost three quarters of Dell's worldwide income. That subsidiary had no actual employees in the Netherlands as of 2009, filings show.

The Dutch company conducts its business through a branch in Singapore (DELL), where it designs and sells laptops and other equipment for the U.S., European and Asian markets.

Singapore Business

For tax purposes, Dell says the unit's profit is generated in Singapore, where it obtained an income-tax holiday in 2004. Although the company pays almost no income taxes in Singapore, the Netherlands doesn't impose any significant income taxes either because "avoidance of double taxation can be claimed with respect to the" profit earned in Singapore, according to the Dutch subsidiary's 2011 annual report.

"You don't want companies to pay double tax but you also don't want them to not pay any tax at all," said Merkies, the Dutch parliament member.

The U.S. Internal Revenue Service is seeking back taxes avoided through Dell's intra-company arrangements, according to a company securities filing. Dell is contesting the IRS's proposed assessment. While the company didn't disclose the amount in dispute, it said an unfavorable outcome could have a "material impact" on its financial position.

Cash Overseas

One result of its tax avoidance: Substantially all of Dell's $14.2 billion in cash and cash equivalents is overseas, according to a company filing in December. It may now have to tap that cash pile as it goes private, potentially subjecting the money to U.S. taxes.

"We've always been clear that Dell has a responsibility to pay its fair share of taxes," said Jess Blackburn, a spokesman for Dell, based in Round Rock, Texas. "We operate according to all applicable laws and regulations and in accordance with the letter and spirit of those laws." He declined to respond to a detailed list of questions about Dell's tax arrangements.

Last month, the European Commission recommended that EU members require in their treaties that income be subject to tax in one country before being exempt in another. That could prevent companies such as Dell from avoiding taxes in two countries simultaneously.

Another EU proposal to combat tax-avoidance strategies has moved slowly through the bureaucracy since 2004. It would allocate multinational companies' taxable profits into various countries based on factors such as actual sales or number of employees there.

'Waiting for Godot'

Whether the EU can implement such a change remains doubtful. Under its rules, the move requires unanimous approval from the 27 member states, including the Netherlands. At a December news conference in Brussels announcing the plan to combat tax avoidance, Algirdas Semeta, the EC's commissioner for taxation, avoided answering a Dutch journalist's question about whether the commission would target the Netherlands.

"I regard the Netherlands as the central European hub in corporate tax avoidance," said Sven Giegold, a member of the EU parliament from Germany's Green Party. "The main challenge is you need consensus within the EU, and waiting for consensus on tax matters is like waiting for Godot."

Last year, representatives from the Netherlands fought at least two internal EU proposals to clamp down on tax avoidance techniques, according to a person familiar with the matter.

Other European countries are competing to attract multinational companies with tax inducements. Luxembourg has imitated the Dutch system of conduit companies and advance tax rulings, and Switzerland offers long-term tax holidays and other incentives.

Swiss Generosity

Yahoo is taking advantage of the Swiss tax generosity: In late 2009, the company began shifting profits from its European sales into a small subsidiary in Rolle, Switzerland, a picturesque town 25 miles north of Geneva at the foot of the Alps.

Through Yahoo! Netherlands BV, headquartered at Dooves's suburban home, Yahoo has also routed European and Asian revenues from Web ads to a subsidiary incorporated in Ireland that claims its residency in the tax-friendly Cayman Islands, according to filings.

In 2009, for example, the Dutch unit collected 101.5 million euros in royalties from around the world -- and promptly paid out 98.7 percent of that to the Cayman subsidiary, records show. If those payments went directly from, say, Yahoo's France sales arm to the Cayman unit, they could trigger a 33.3 percent withholding tax in France.

'Beneficial Owner'

In 2011, a Yahoo French sales subsidiary reported 66 million euros of revenue, yet paid just 462,665 euros in income taxes, records show.

A typical Dutch tax avoidance arrangement may violate the tax treaties of various countries, said Peters, the Rotterdam tax adviser. Only a small percentage of royalties stays in the Netherlands in these transactions, records show, yet treaties typically require that, in order to avoid withholding tax, the Netherlands unit must be the "beneficial owner."

"It's clearly visible in the public accounts in Holland that these Dutch entities are not the beneficial owners," said Peters, speaking generally about such arrangements.

Yahoo recently introduced another circuitous path through the Netherlands to cut the taxes on profits from its Asian sales: Royalties travel from Singapore, through Dooves's house, to another subsidiary in Mauritius, a tax-friendly island off the southeast coast of Africa.

In 2011, the Dutch unit collected 110 million euros from Asian sales, according to Dooves -- before paying royalties to the Mauritius subsidiary.

On paper, the cash remains with the Dutch subsidiary, which uses it to finance operations throughout the world outside the U.S., said Dooves. In reality, much of it sits in a HSBC Holdings Plc bank account in London, he said.

To contact the reporter on this story: Jesse Drucker in Rome at jdrucker4@bloomberg.net

To contact the editor responsible for this story: Daniel Golden in Boston at dlgolden@bloomberg.net